

SUMMARY ANALYSIS OF AMENDED BILL

Franchise Tax Board

Author: Figueroa Analyst: Jeani Brent Bill Number: SB 495

Related Bills: None Telephone: 845-3410 Amended Date: May 6, 1999

Attorney: Patrick Kusiak Sponsor:

SUBJECT: Employer New Full-Time Space Vehicles, Parts, Satellites, and Equipment
Employee Credit

DEPARTMENT AMENDMENTS ACCEPTED. Amendments reflect suggestions of previous analysis of bill as introduced/amended _____.

AMENDMENTS IMPACT REVENUE. A new revenue estimate is provided.

AMENDMENTS DID NOT RESOLVE THE DEPARTMENT'S CONCERNS stated in the previous analysis of bill as amended April 13, 1999.

FURTHER AMENDMENTS NECESSARY.

DEPARTMENT POSITION CHANGED TO _____.

REMAINDER OF PREVIOUS ANALYSIS OF BILL AS AMENDED April 13, 1999 STILL APPLIES.

OTHER - See comments below.

SUMMARY OF BILL

Under the Personal Income Tax Law and the Bank and Corporation Tax Law, this bill would allow a credit of \$1,000 for each qualified new employee employed by the taxpayer in California during the taxable or income year and primarily engaged in activities related to space vehicles and parts and space satellites and equipment.

SUMMARY OF AMENDMENT

The May 6, 1999, amendments:

- added the requirement that the qualified employee perform the qualified services in California;
- added the requirement that the qualified employee be *primarily* engaged in activities related to aerospace;
- specified that a new employee shall not include any person currently employed in California by the taxpayer's corporate parent, subsidiary, or affiliated entity; and
- added a sunset date of January 1, 2007.

The amendments also required the California Research Bureau to report to the Legislature by January 1, 2005, on the number of taxpayers claiming the credit, the amount of credits claimed, and the number of new jobs created in the aerospace industry as a result of the credit. The Franchise Tax Board (FTB) and the Employment Development Department (EDD) would be required to provide information necessary to complete the report.

The addition of the first two requirements eliminate the policy concerns and the first implementation concern in the department's analysis of the bill as amended April 13, 1999. The amendments created implementation and technical concerns,

Board Position:

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Department/Legislative Director Date

Johnnie Lou Rosas 5/14/1999

which are provided below with the two implementation concerns from the department's prior analysis. The remainder of the department's prior analysis still applies.

Implementation Considerations

By providing that "qualified employee" includes employees employed less than three years, it appears that the intent would be to allow the taxpayer to take the credit for the first three years of employment of that employee. However, the bill also states that "qualified employee" shall not include any person previously employed by the taxpayer within the year prior to the taxable or income year, which appears to disallow the second and third years of the credit. Therefore, it is unclear whether the author intends that taxpayers would be allowed the credit for three years of employment or only for the first year in which the employee is employed.

This bill states that a "new" employee is one who fills a "newly created position." This requirement leaves unclear whether the position must be newly created in the current taxable or income year or some earlier income or taxable year and whether the "new employee" must be the first employee to fill that position.

The credit could be carried over indefinitely past the repeal date. Recently enacted credits have contained a limit on the carryover since most credits are exhausted within eight years. A limit allows the department to eventually remove the credit from the tax returns.

The amendment requires the FTB to provide information to the California Research Bureau necessary to enable the Bureau to complete its report to the Legislature concerning the credit. The FTB would provide this data on an aggregate basis for all SIC codes referenced in the bill. Due to the relatively small number of taxpayers in segments in this industry, supplying the information on a specific SIC code basis may constitute the disclosure of confidential tax information.

The addition of the prohibition against the hiring of any person "currently employed in this state by a taxpayer's corporate parent, subsidiary, or any other affiliated entity" may be difficult for the department to administer due to the difficulty in determining whether an employee is "employed in this state" and also because it is unclear when the determination of "currently employed in this state" should be made. If the language is to be interpreted literally, it appears that a long-term employee could be moved out of California for literally a day or a week and not be treated as "currently employed in this state."

The amendment added the requirement that an employee be engaged in activities "primarily" related to space vehicles and parts, and space satellites and equipment, but does not define "primarily." Under the Manufacturers' Investment Credit, "primarily" is specifically defined to mean "50 percent or more" (R&TC Sec. 23649(e)(5)). Clarification of the author's intent would avoid disputes between taxpayers and the department as to the meaning of this term.

It is unclear what would constitute an "affiliated entity" for purposes of the prohibition against the hiring of any person employed by a taxpayer's "corporate parent, subsidiary, or any other affiliated entity." A federal law definition of "affiliated entity" generally uses an 80% ownership threshold, while R&TC Section 25105 uses an 50% ownership threshold to define a commonly-controlled group. Clarification of the author's intent, or substitution of a "related party" rule similar to that contained in Sections 267, 318 and/or 707 of the Internal Revenue Code, would avoid disputes between taxpayers and the department as to the meaning of this term.

Technical Considerations

The credit would be repealed as of January 1, 2007, which would disallow the credit for the 2006 year for fiscal year filers, even though calendar year filers could claim it for the year. Amendments 1 and 2 would change the repeal date to December 1, 2007, to allow fiscal and calendar year taxpayers to claim the credit for the same years.

LEGISLATIVELY MANDATED REPORTS

The California Research Bureau would be required to report on this credit by January 1, 2005. The FTB and EDD would be required to provide any necessary information to the Bureau.

BOARD POSITION

Pending.

At its March 23, 1999, meeting, the Franchise Tax Board voted 2-0 to take a neutral position on this bill as introduced February 18, 1999. The Board has not had the opportunity to review the recent amendments.

Analyst	Jeani Brent
Telephone #	845-3410
Attorney	Patrick Kusiak

FRANCHISE TAX BOARD'S
PROPOSED AMENDMENTS TO SB 495
As Amended May 6, 1999

AMENDMENT 1

On page 3, strikeout lines 16 to 18, and insert:
December 1, 2007, and as of that date is repealed.

AMENDMENT 2

On page 4, strikeout lines 30 to 32, and insert:
December 1, 2007, and as of that date is repealed.